Service Date: June 7, 1996

DEPARTMENT OF PUBLIC SERVICE REGULATION BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MONTANA

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IN THE MATTER OF MONTANA-DAKOTA)	UTILITY DIVISION
UTILITIES COMPANY, Application for)	
Authority to Increase Rates for)	DOCKET NO. D95.7.90
Natural Gas Service in Montana.)	ORDER NO. 5856d

ORDER ON RESERVED ISSUE

- 1. In a November 24, 1995 Notice the Commission created a reserved issue involving an interconnect of MDU's distribution system with MPC's gas transportation system in Billings. Based on the parties' testimony, the interconnect issue evolved to include rate design. For this reason, the Commission first reviews Rate 84's history. After this review the respective intervenor and MDU testimonies from the main and the reserved issue cases are summarized. A Commission decision concludes this order.
- 2. Rate 84 allows customers to take firm transportation service over MDU's distribution system. Customers that use Rate 84 must independently acquire and arrange for delivery of gas to MDU's distribution system. Thus, if the rates are cost-based, Rate 84 is one component of an open access gas transportation system. Firm transport Rate 84 was conditionally approved in Docket No. 88.11.53 (Order No. 5399b, FOF-285). The MCC did not testify on Rate 84 issues in Docket No. 88.11.53. MDU's Base Rates and a \$1.325/dkt commodity price were approved.
- 3. Rate 84 was at issue again in Docket No. 88.8.23. MCC testified on Rate 84 issues in this docket. MDU proposed a "margin-based" Rate 84 tariff with a commodity price of about

- \$1.37/dkt (Order No. 5490, FOF 138, 142). MCC held that MDU's Rate 84 was unsound and that the margin may <u>understate</u> costs. After linking rate design and gas acquisition strategies, MCC recommended eliminating Rate 84 (id, FOF Nos. 144-147).
- 4. The Commission approved Rate 84 but only after correcting the tariff to exclude MDQ and AEQ charges contained in MDU's margin approach (id, FOF 153). Although it found firm transport to be one means to improve efficient gas use on MDU's distribution system (Order No. 5490, FOF 178), the Commission expressed concern with the discriminatory design of Rate 84. This concern regarded how MDU effectively allocated ten times more distribution demand costs to Rate 84 than to firm sales Rate 70 (id, FOF 155). As for MDU's proposal to limit access to Rate 84, the Commission found merit in MCC's testimony to not restrict the offering to just interruptible customers. The Commission found debatable whether firm commercial customers should have access to Rate 84 (id, 178).
- 5. The Commission received MDU's next cost of service and rate design filing in Docket No. 92.2.9. That docket was combined with other MDU dockets (Nos. 93.4.15 and 93.4.19). The

¹ MDQ and AEQ were Williston Basin Pipeline's charges assessed firm transport customers. MDQ and AEQ respectively mean maximum daily and annual energy quantities.

 $^{^{2}}$ Prior to receipt of DEQ's testimony in this docket MDU asserts to have corrected all past Commission concerns (MDU Data Response No. PSC-26).

combined dockets addressed open-access discrimination issues referred from Docket No. 88.8.23. The settlement docket (No. 94.4.17) approved MDU's margin-based Rate 84.

- 6. <u>Direct Testimony: Main Case</u> The Montana Department of Environmental Quality (DEQ) testimony on an interconnect with MPC's gas system, in part, gave rise to this reserved issue.
- 7. The stated purpose of Mr. Frantz's (DEQ's) September 1995 direct testimony is to explore an interconnect between MDU and MPC at Billings. He suggests the interconnect would allow MDU and, or, its customers to have access to gas supplies and services available to other customers using MPC's system. In asserting an interconnection is inexpensive, he recommends an interconnect to retain customers and to increase the benefits of competition.
- 8. Mr. Frantz attributes MDU's customer losses to rate design but disagrees with MDU as to the sources of the Company's losses. He identifies Williston Basin Interstate Pipeline's rates as the <u>primary</u> source of MDU's load loss adding that the exclusive relation between affiliates disables MDU's ability to compete with alternative gas providers. As a solution, Mr. Frantz holds that customers should have the option of firm MDU service (a.k.a. Rate 84) combined with MPC as a source of gas. Thus, MDU should seriously explore an MPC interconnect.
- 9. Mr. Frantz is concerned with the relation between MDU's firm and interruptible transport rate levels and advises the Commission to revisit the basis of MDU's rates (Direct, pp. 4-8).

In testifying that MDU has no apparent distribution capacity shortage, and interruptible service provides little value, he argues that MDU's firm transport service rate could be lowered and interruptible transport rates increased. In lieu of their

present retention basis, rates should reflect the value of benefits.

- 10. MDU's Reserved Issue Direct Testimony Mr. Don Ball's December 6, 1995 reserved issue testimony opposes an MDU interconnect with MPC. His opposition ties to the avoidability of costs for the three cost functions (field gas, transmission and distribution). Of the functions involved in supplying gas to the burner tip, he asserts an interconnect will not allow for distribution cost avoidance. He asserts the facility costs of an interconnect would have to be borne by an individual customer and adds that such duplicative facilities are wasteful.
- 11. As for the field cost of gas (production), Mr. Ball asserts there is little difference between MPC's and MDU's average price of gas, as reflected in recent gas tracker adjustment filings. In fact, MPC's average price may exceed MDU's. Therefore, the interconnect idea must focus on transmission costs.
- 12. In turn, Mr. Ball addresses the avoidability of Williston Basin Interstate Pipeline costs and Mr. Frantz's reasoning that an interconnect will cause Williston Basin Interstate Pipeline to lower its prices. As with distribution, Mr. Ball asserts Williston Basin Interstate Pipeline's

Ms. Aberle's October testimony in the main case rebuts the rate design aspects of Mr. Frantz's testimony. She disputes his assertion that customers switching from firm sales to firm transport will not affect other rates. His proposal to further reduce the Firm transport (Rate 84) rate breaks the tie between firm transport and firm sales rates and thus causes remaining sales customers rates to rise. Such a reduction would also lower MDU's average rate of return on investment below an acceptable level, relative to MDU's proposed Rate 84 price of \$1.036/dkt. Although MDU's flexibly-priced interruptible rates serve as retention rates, she adds that if a flexibly priced rate retains a customer all customers benefit.

transmission costs are not avoided. While a bypass customer taking MPC gas may temporarily reduce its costs, other core customers' rates must rise to offset the Williston Basin Interstate Pipeline costs previously recovered by that customer. If MDU reduced its capacity reservation, due to an interconnect, Williston Basin Interstate Pipeline will just raise its rates to its remaining customers.

- 13. Mr. Ball adds that Mr. Frantz's expectation that an interconnect will cause Williston Basin Interstate Pipeline to lower its transport rates, reveals a substantial lack of knowledge about ratemaking and interstate pipeline operations. Mr. Ball asserts there will be no effect on Williston Basin Interstate Pipeline's total cost of providing firm transport service: a rational interstate pipeline will not discount rates if it can recover the full cost of providing firm capacity. He doubts MPC has firm capacity, as Mr. Frantz assumes, adding that MPC's firmest capacity is actually interruptible on peak.
- 14. As for public policy concerns, Mr. Ball asserts Mr. Frantz's proposal disadvantages core customers in favor of a few large bypassing customers (e.g., State of Montana). He adds that Mr. Frantz's proposal also favors MPC's customers over MDU's customers. While not opposed to open access the obligation to serve emerges as another MDU policy concern. As a matter of policy, MDU holds it should not bear an interconnect's cost and ratepayers must be protected from the impacts of bypass. Protection must include exit fees to protect the core market. The elimination of cross subsidies should precede open access. As for reciprocity, if MDU must build an interconnect, so must all other jurisdictional utilities if required.
- 15. <u>DEQ's Reserved Issue Direct Testimony</u> In concern over MDU's loss of firm customer loads, Mr. Frantz asserts an

interconnect between MDU and MPC would mitigate load loss and would enhance competition between Williston Basin Interstate Pipeline and MPC. As an interconnect's feasibility relates to the level of MDU's Rate 84, he computes and discusses the impact of a lowered Rate 84 price. An interconnect's feasibility is critically linked to the recovery of both stranded and interconnection costs, and the availability of MPC capacity.

16. Mr. Frantz testifies that Rate 84 is computed incorrectly. If computed based on the margin approach, as MDU asserts, Rate 84 is inconsistent with other interruptible transport rates. To correct Rate 84 the revenues from Base Rates must be subtracted from the Rate 84 transport price. If corrected, Rate 84 drops to about \$.706/dkt. He asserts that a high Rate 84 transport price causes firm sales customers to cease service (id, p. 3). In assuming fifty firm general service (Rate 70) customers, each with an average consumption of 1,517 Dkt, switched to Rate 84, he computes a windfall revenues in the amount of \$100,002 (id, p. 8). Increased Rate 84 volumes would serve to hold down core customers' rates.

⁴ In its final order (No. 5490) in Docket No. 88.8.23 the Commission questioned MDU's effective allocation of ten times more distribution demand costs to Rate 84 than to Rate 70.

- 17. The impact of lowering Rate 84 is complex and involves Williston Basin Interstate Pipeline stranded costs that arise when a customer shifts tariffs. Mr. Frantz recites MDU's \$.262/dkt stranded cost estimate when customers switch from interruptible to firm transport. While agreeing that stranded costs will arise he asserts that the expiration of contracts with Williston Basin Interstate Pipeline allows for stranded cost mitigation. Revenue over-collections from Rate 84 sales could also mitigate stranded costs.
- 18. As for cost recovery and contrast to past MDU analyses, Mr. Frantz testifies that in an interconnect's cost should be borne by those who use it. He asserts MDU's past (Rate 88 tracker) interconnect cost estimates wrongly passed through costs to core customers. Since core customers will not apparently use the interconnect they should not, initially, bear the cost (id, p. 3). Since customers that bypass MDU via propane standby systems directly incur such costs, he expects other customers will happily assume an interconnect's costs. As the status quo involves redundant "standby fuel systems" combined with MDU's interruptible rates, it is not socially or economically efficient. Once in place, an interconnect would minimize the shift of fixed costs to core customers. Therefore, he urges the Commission to further study an interconnect between MDU and MPC.
- 19. An interconnect's merit also depends on MPC's capacity to deliver firm gas consistent with Rate 84's firm quality of service. Mr. Frantz interprets a data response from MPC's Ms. Karen Schellin to mean MPC has sufficient capacity on its "line"

⁵ MDU asserts stranded investments arise when customers bypass MDU's system but not when they switch from sales to transport service (MDU Data Response to PSC-29).

to serve MDU customers in the Billings area (in MPC Docket No. D95.9.128, DR No. DEQ-13). He assumes, however, MPC can and will interrupt other large loads served by the Shoshone line so that other MDU customers can take firm service. He also assumes MPC would adjust its system if sufficient customer interest emerged for firm supplies into Billings.

MDU's Reserved Issue Rebuttal Testimony Ball's February 12, 1996 testimony rebuts three aspects of Mr. Frantz's testimony. First, since firm sales customers (Rate 70 General Service customers) cannot access firm transport Rate 84 service, it is not possible, as Mr. Frantz asserts, that a high Rate 84 price caused MDU to lose firm sales customers. Rate 84 is only available for the firm requirements of interruptible customers. Second, Mr. Ball now concedes that Rate 84 double collects certain revenues and should now be modified, but rebuts Mr. Frantz's proposal to lower the commodity charge. Since Rate 84 double collects Base Rates, Mr. Ball would retain MDU's proposed commodity rate and remove tariff language suggesting that a Base Rate still applies. If Mr. Frantz's commodity charge was approved, a separate Base Rate(s) must apply. Ball disagrees with Mr. Frantz's suggestion that an over collection of revenues occurs with Mr. Frantz's lower commodity Once more, Mr. Ball asserts that because Rate 70's firm sales customers cannot take Rate 84 firm transport service, any over collection is simply due to Mr. Frantz's misunderstanding. Mr. Ball asserts Mr. Frantz has no idea of the cost of an MDU interconnect with MPC or whether MPC has firm capacity.

Commission's Reserved Issue Decision

21. Because the Commission has decided the Rate 84 pricing issues (Final Order No. 5856b), the reserved issue largely involves the interconnection with MPC's system in Billings.

Aside from having eliminated the double collection of base rates, the Commission is not yet confident that Rate 84 is cost-based. However, as noted in the final order (No. 5856b), the cost basis of Rate 84 and other rates must await MDU's next cost of service and rate design docket.

- 22. Although DEQ's testimony is insightful, the Commission is concerned with the resulting piecemeal approach to optimizing the use of gas resources on MDU's system. While DEQ identifies Williston Basin Interstate Pipeline as the primary source of MDU's load losses, other concerns remain unresolved. Other concerns involve open access, unbundling and customer aggregation. That said, the Commission will address the interconnect issue.
- 23. Indeed, Williston Basin Interstate Pipeline casts a shadow over the competitiveness of gas transportation on MDU's system. While the ideal solution lies in a bypass option for MDU's entire customer base, increased competition in the Billings area could be beneficial. The Commission is not convinced that it is timely to require MDU to do further analyses. Others such as MPC, or even a third party, could study and provide an interconnect. Ordering MDU to interconnect with MPC is premature and possibly a flawed policy at this time. Why not order MPC, or even Great Falls gas, to study an interconnect?
- 24. Further analysis needs to occur in an MPC docket before further studying the interconnect from MDU's perspective. Although it may turn out to be wishful thinking, there is hope that others will recognize and exploit any apparent economic opportunities on MDU's system. In any case, the Commission intends to explore the availability of MPC pipeline resources in the MPC consolidated docket filed this July 1996 (Docket No. D96.2.22). Once the Commission has exhausted the opportunity to

expand its knowledge in that docket, a link between the two dockets may be forged and more deliberate public policy pursued in a subsequent MDU docket. As the Commission can only conjecture that an interconnect generates net benefits it intends to better understand the impacts of any interconnect on captive MDU customers. Whether an interconnect that simply shifts costs to other customers is efficient needs to be explored. It is not, however, clearly inefficient if the freed up capacity has alternative uses. Also, unresolved is the magnitude and responsibility of "exit fees" to assumably recover any stranded costs.

- 25. Therefore, the Commission alerts MDU to the expectation that the Commission will further explore the net benefits of an interconnect. This is consistent with DEQ's testimony. However, the Commission finds premature an order that MDU perform that study now.
- 26. By this action the Commission does not intend to preclude MDU, any party or any interested person from advising the Commission at any time, of any concerns, thoughts or suggestions on this matter, whether those relate to substance or procedure.

DONE AND DATED THIS 6th day of June, 1996, by a vote of 5-0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

NANCY McCAFFREE, Chair	
DAVE FISHER, Vice Chair	

BOB ANDERSON, Commissioner

DANNY OBERG, Commissioner

BOB ROWE, Commissioner

ATTEST:

Kathlene M. Anderson Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.